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C O N F I D E N T I A L SECTION 01 OF 02 TEL AVIV 004728

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SUBJECT: (C) ISRAEL CONSIDERS WITHDRAWING FROM GOVERNMENT
PROCUREMENT AGREEMENT

REF: GENEVA 01508

Classified By: Ambassador Daniel C. Kurtzer for reasons 1.4 (b) and (d)

11. (C) Summary. The Ministry of Industry, Trade, and Labor (MOITL) is considering withdrawing from the Government Procurement Agreement (GPA) if the GOI is unable to maintain offsets at the current level. MOITL staff claim that economic analysis and industry advocacy have made it clear that costs of remaining a member of the GPA if offsets are reduced are far higher than any benefits that Israel gains from the agreement. Israeli officials are beginning lobbying efforts to maintain 30% offset commitments on government contracts. End summary.

12. (C) In a July 5 meeting to discuss WTO issues Yair Shiran, Director of International Agreements and Trade Policy, and Yoram Zara, Director of Multilateral Agreements Division (and primary POC for WTO issues) from the Ministry of Industry and trade expressed their view that Israel derives limited benefits from being a member of the GPA, and that maintaining offset commitments at the current level was the only way to assure continued GOI participation. In addition, Shiran commented that the United States "could be of great help" on this issue, and that "progress (on offsets) might make other issues easier to resolve."

13. (C) The MOITL staff held a high-level meeting with the Director General of MOITL the evening of July 5 to discuss a negotiating strategy and next steps for the GOI in the GPA.

14. (C) Despite the professed "cost" of the agreement for the GOI (if they are not able to maintain offsets at current levels), staff at MOITL were unable to answer a number of questions posed by Econoff related to their participation in the GPA. The questions included:
-What have industries that are interested in selling security equipment to the Department of Homeland Security said about the agreement?
-What is the total cost to the GOI (budget) from maintaining offsets?
-If the theory behind offsets is to increase the number of contacts between Israeli companies and large multi-nationals that win government tenders, why is there a need to maintain this restriction 10 years after the market opened? Have the business relationships not already been formed?
-What benefit do Israeli SMEs gain when multinationals are allowed to offset their government contracts with investment in a local subsidiary?

15. (C/NF) The question of fulfilling offset requirements by establishing local subsidiaries has potentially the most devastating impact on the GOI justification for maintaining offset requirements. During meetings of the Forum of American Companies Procurement Committee (held under the auspices of the Israeli-American Chamber of Commerce) post first became aware of the use of "umbrella agreements" to satisfy offset requirements. Large American companies that won multiple government contracts in 2004 received messages in the first quarter of 2005 that they had failed to fulfill their offset requirements from the previous year. In order to bid on new government tenders, the companies were encouraged to sign umbrella agreements that count planned investment in Israeli subsidiaries or manufacturing plants as part of the mandated 30% offset requirement on all future government contracts. In a move to extend these guarantees the MoF extended the terms of the umbrella agreements over the space of 3-5 years. However, no American company was willing to go on the record regarding their umbrella agreement with the GOI, in part because of fear of future discrimination when bidding on GOI government contracts. To date, however, most of the companies have been satisfied with umbrella agreements because many already had planned to expand investment in Israel, and this method of accounting for offsets simplified their business strategy. None of the companies on the Forum of American Companies Procurement Committee seemed to be aware that the GOI had been approved for only a one year extension of 30% offsets.

16. (C) When queried about the possible benefit for the GOI if

they withdraw from the GPA, MOIT's Zara noted that under Israeli law the government is allowed to seek offsets up to a 35% value of many government tenders. It is possible that Israel could actually increase the level of offsets imposed on international companies that win government tenders. The GOI's position is troubling given the present negative climate for government procurement in Israel.

17. (SBU) Comment. The Forum of American Companies Procurement Committee, in coordination with Post economic and commercial officers has identified a number of problems that prevent fair competition in government tenders in Israel.

- Lack of a central clearinghouse for publication and notification of tenders (similar to FedBizOpps);
- Lack of an Ombudsman to act as government-wide POC for companies with questions and complaints;
- Unlimited corporate liability clauses that prohibit U.S. companies' participation or increase the cost of participation through higher insurance costs;
- Lack of a neutrality policy and use of unnecessarily restrictive standards in government tenders.

18. (C) Comment continued. The Ministry of Finance has made a commitment via the Loan Guarantee Commitment Agreement to address USG concerns on procurement issues. The final draft of the Loan Guarantees Agreement, Appendix 6, Section 6 commits the GOI to, "work with the U.S. Government to resolve outstanding procurements and standards issues." This agreement was signed less than one week ago by Joseph Bachar, Director General of the Ministry of Finance. To date the GOI has made limited progress in resolving USG concerns. The willingness on the part of MOITL staff to consider withdrawal from an international agreement may signal a hardening of positions that the GOI will adopt on other sensitive trade issues. End comment.

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